

**MINUTES
of the
THIRD MEETING
of the
NEW MEXICO FINANCE AUTHORITY OVERSIGHT COMMITTEE**

**August 20-21, 2012
The Science and Technology Park Rotunda
University of New Mexico
Albuquerque, NM**

The third meeting of the New Mexico Finance Authority (NMFA) Oversight Committee was called to order by Senator Mary Kay Papen, chair, on August 20, 2012 at 10:15 a.m. at the University of New Mexico's Science and Technology Park Rotunda.

Present

Sen. Mary Kay Papen, Chair
Rep. Patricia A. Lundstrom, Vice Chair
(8/20)
Rep. Alonzo Baldonado
Sen. Sue Wilson Beffort (8/20)
Sen. Stephen H. Fischmann
Rep. Roberto "Bobby" J. Gonzales (8/20)
Sen. Clinton D. Harden, Jr.
Rep. Yvette Herrell
Rep. Dona G. Irwin (8/20)
Sen. Howie C. Morales (8/20)
Rep. Jane E. Powdrell-Culbert
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Rep. Henry Kiki Saavedra (8/20)
Sen. David Ulibarri
Rep. Richard D. Vigil (8/20)
Rep. James P. White

Advisory Members

Rep. Ernest H. Chavez
Rep. Anna M. Crook
Rep. Mary Helen Garcia
Sen. Mary Jane M. Garcia
Rep. Thomas A. Garcia (8/20)
Rep. Rick Little
Sen. Lynda M. Lovejoy
Sen. Richard C. Martinez

Absent

Sen. Tim Eichenberg
Rep. Candy Spence Ezzell
Rep. James R.J. Strickler

Sen. William F. Burt
Rep. David L. Doyle
Sen. Eric G. Griego
Rep. Ben Lujan
Sen. George K. Munoz
Sen. Steven P. Neville
Sen. William H. Payne
Rep. Thomas C. Taylor

Rep. W. Ken Martinez
Rep. Andy Nuñez (8/20)
Rep. Edward C. Sandoval (8/20)
Rep. Sheryl Williams Stapleton (8/21)

Guest Legislator

Sen. Timothy M. Keller (8/20)

(Attendance dates are noted for members not present for the entire meeting.)

Staff

Lisa Sullivan, Legislative Council Service (LCS)
Doris Faust, LCS
Tom Pollard, LCS
Elizabeth Shaw, LCS

Guests

The guest list is in the meeting file.

Handouts

Handouts and other written testimony are in the meeting file and are posted on the New Mexico Legislature web site.

Monday, August 20

Senator Papen welcomed committee members, presenters and guests and asked that the committee members introduce themselves. She then introduced the first presenters, Nann Winter, chair of the NMFA Board, and John Gasparich, interim and acting chief executive officer (CEO) of the NMFA.

NMFA Status Report on Bond Ratings

Ms. Winter provided the committee with a copy of Mr. Gasparich's resumé and gave an overview of her own credentials and work history. Mr. Gasparich stated his goals for the NMFA, which are: to return the NMFA back to the business that it is intended to be in, namely providing loans to the cities and towns in New Mexico; and to aid in the restoration of the NMFA's bond rating.

After Mr. Gasparich addressed the committee, Ms. Winter gave an overview of the last 30 days of activity within the NMFA. She informed the committee that in regard to the false audit, the Office of the State Auditor (OSA) chose the accounting firm PricewaterhouseCoopers to conduct the forensic investigation under its direction. The cost of services performed by PricewaterhouseCoopers will be paid out of the NMFA's operating budget. The NMFA Board canceled the contract with the law firm Steptoe and Johnson, LLC to perform substantially

similar services. An NMFA task force was formed to develop a new scope of work for the forensic investigation. She stated that there would be three concurrent investigations. She highlighted the most recent NMFA Board actions at its meeting on August 17, 2012, where the board appointed Mr. Gasparich as the interim and acting CEO of the NMFA and entered into a \$1.25 million contract with PricewaterhouseCoopers.

Committee members raised concerns as to whether the engagement of PricewaterhouseCoopers was done through the request for proposals (RFP) process or whether it was a sole-source contract. Ms. Winter responded that, due to the sensitivity of the situation, there was not time to go through the RFP process, and because of its status, the NMFA is able to enter into a contract on an emergency basis, which is what was done in this case.

Ms. Winter introduced Michael Zavelle, chief financial strategist of the NMFA, to the committee. Mr. Zavelle provided the committee with a handout that outlined the key rating factors that are taken into account by ratings agencies with respect to the Public Project Revolving Fund (PPRF). He informed the committee that the NMFA was set up in such a way as to keep it independent of the state, and while the NMFA is experiencing the problem of the false audit, a change in NMFA bond ratings would not affect state bond ratings. Similarly, while the Department of Transportation (DOT) sometimes has bonds issued through the NMFA, the DOT's credit rating will not be impacted should the NMFA's bond ratings change.

Mr. Zavelle then described the possible effect of a false audit on the NMFA's bond ratings. Upon speaking with the bond ratings agencies Moody's and S&P, Mr. Zavelle was left with the impression that while the agencies are concerned with whether the audit is timely and accurate, the false audit alone would not serve as the reason for a downgrade. Ratings agencies understand that audit reports are compilations of financial information that are out-of-date by the time reports are filed. Mr. Zavelle stated that what is most valuable to the ratings agencies is current information; for example, what is in the Debt Services Reserve Fund, and how is management performing? The biggest detriment that a false audit has with respect to the ratings agencies is the loss of credibility and the reflection of inadequate governance practices. Once the ratings agencies are satisfied that all of the NMFA's current information is correct, they will resume examining the fiscal solvency and governance practices of the NMFA. Mr. Zavelle stated that the best road to recovery is through complete disclosure.

In response to committee members' questions, Mr. Zavelle stated that when a ratings agency is evaluating the NMFA, the audit is not of the highest importance; what is most important is current information, including bond payments. He stated that while he remains uncertain of the future for the NMFA's bond ratings, generally speaking, if an agency's last bond rating was raised, then its subsequent rating also should rise. Two of the most important factors in the maintenance of the NMFA's current bond ratings will be the timelines and perceived quality of the investigation.

He then directed the committee members' attention to the PPRF program. He then explained the percentage of the NMFA governmental gross receipts tax share allocated to the PPRF. He also explained the purpose of the Debt Service Reserve Fund and intercepted revenues, and how each plays an important role in the NMFA's bond rating. Committee members then questioned Mr. Zavelle on whether he could point to the successful loan repayments when in a meeting with ratings agencies. He stated that there had been no defaults, and this was also a key reason for the NMFA's high rating.

Committee members then discussed the role of the firm Clifton Gunderson, which was supposed to have performed the 2011 external audit, and they asked Mr. Zavelle if that firm conducted prior external audits for the NMFA. Mr. Zavelle responded that Clifton Gunderson was used in 2009 and 2010.

Committee members then addressed concerns about the governance of the NMFA Board and directed questions to Ms. Winter about potential conflicts of interest and whether she has any current clients that work with the NMFA. She replied that while many of her clients have discussed or done business with the NMFA, she is keenly aware of conflicts of interest. Should any of her clients come before the board, she would recuse herself from voting. There was some discussion among the committee members as to the possibility of having an election of the chair by the NMFA Board, rather than appointment by the governor. The committee then addressed Mr. Gasparich and asked his intention of remaining with the NMFA, to which he responded that he would remain with the NMFA through the upcoming legislative session.

Committee members then asked Mr. Zavelle to explain reverted funds. Mr. Zavelle informed the committee that a number of reverted funds are from the GRIP 2 program, not to be confused with the GRIP bond program, and that this information has been made available to the ratings agencies and is also available on the NMFA web site.

Committee members also asked about the funds that were taken from the NMFA and placed in the general fund. Mr. Zavelle replied that over the past couple of years, \$47 million had been transferred by the legislature from NMFA funds to the general fund.

Committee members raised concerns about the treatment of NMFA staff during the criminal investigation and displayed their displeasure at the treatment of those individuals who were arrested. The committee questioned Ms. Winter as to Rick May's status within the NMFA and how long his leave with pay would continue. To this, Ms. Winter was unable to reply.

NMFA Status of Available Cash Balance in PPRF and Report on Interest Rates and Loan Terms Available to Municipalities

Mr. Zavelle told the committee that there is currently \$34 million in the PPRF with a projected \$3 million in loans per month that will see the NMFA through March 2013, when more funding is expected to become available. Committee members asked which projects would be delayed. Mr. Zavelle directed them to the project pipeline on the NMFA web site.

Mr. Zavelle stated that the critical portion of the state audit is expected to be completed in 30 to 40 days, and more information should be available by October 31, 2012. He informed the committee that the 2011 audit is expected to be completed by November 31, 2012, and the 2012 audit should be completed by the end of January 2013. With the completion of the 2012 audit in January 2013, the NMFA will be able to issue new bonds, and funding should become available in March 2013.

Committee members inquired about the NMFA's current financial information. Mr. Zavelle replied that all financial information for the NMFA is up to date and a plan is in place to post a quarterly report on the NMFA web site. A motion was then made and seconded to require the NMFA to provide the committee with a quarterly financial report for the committee to determine the authority's health and maintain oversight.

On the subject of loan terms and interest rates available to municipalities, committee members questioned Mr. Zavelle as to why, under the PPRF, the NMFA requires an audit from a community before it makes a loan. Mr. Zavelle informed committee members that this policy was developed by the NMFA to protect the PPRF, and because of this policy, a number of communities have been making steps toward maintaining a current audit. Committee members continued to raise concerns about small rural communities that cannot afford to retain an auditor to perform the audit.

NMFA Temporary Protocol for PPRF Loans

Mr. Zavelle then directed the committee's attention to a handout regarding the recommended temporary protocol for lending from PPRF cash balances until the NMFA next issues PPRF bonds. He stated that the goal of the protocol is first to serve the smaller New Mexico communities that have the least access to competitive loan interest rates and to encourage larger municipal entities that have that access to seek non-NMFA loans. The protocol requires that new PPRF loans should be for infrastructure projects only and not for refunding or refinancing existing loans. He stated that since NMFA policy requires loans of \$5 million or more to be funded simultaneously with the issuance of bonds, until bonds can again be issued, PPRF loans should be restricted to infrastructure projects of less than \$5 million in size. He also informed the committee that public health, safety or other compelling needs will override basic protocol as approved on a case-by-case basis by the NMFA Board.

Committee members raised questions about the cash balances outside of the PPRF and also the current operating budget of the NMFA. Mr. Zavelle responded that only cash in the PPRF could be used for making PPRF loans approved by the legislature.

In response to committee members' questions about the current operating budget, Mr. Zavelle informed the committee that the budget for fiscal year 2012 was \$8.5 million, and the funds to pay for the audit will come from the operating budget.

Forensic Examination and Investigation

Daniel S. Tanaka, director of the Securities Division of the Regulation and Licensing Department, introduced himself to the committee and gave some background on himself and his agency. He stated that his office is swiftly conducting a criminal investigation into the alleged fraudulent audit and transfer of NMFA fund balances to the general fund.

In answer to committee members' questions, Mr. Tanaka stated that the division has been working closely with Mr. Balderas' office and is willing to provide his office with any information that might be needed. Mr. Tanaka also indicated his willingness to cooperate with the legislature's investigator.

Hector Balderas, state auditor, provided the committee with an overview of events and outlined three objectives that his office has: to perform a forensic examination concerning the alleged fraudulent audit; to oversee the completion of the NMFA's 2011 and 2012 financial audits; and to work with the LCS on the NMFA Oversight Committee's independent review of the NMFA. Mr. Balderas agreed that the NMFA should complete its 2011 and 2012 audits as soon as the critical part of the forensic examination is finished and it receives direction from the OSA so that the NMFA does not fall further behind on its audits.

Mr. Balderas distributed a handout that outlines a scope of work of the forensic examination that will focus on areas of risk and why audit procedures were not followed. He confirmed that PricewaterhouseCoopers has agreed to perform the forensic examination and the NMFA has approved the transfer of funds to pay for it.

Committee members raised concerns about the steps that Mr. Balderas' office is taking to ensure that something of this nature does not occur again in the future. Mr. Balderas replied that his office is attempting to mandate an audit compliance training for state agencies. He stated that during November and December, his office receives approximately 500 to 600 audit reports, and if an agency misses a deadline, the responsibility falls on each agency's management and oversight boards. Mr. Balderas informed the committee that while his office has the ability to notify an agency that it is in default, there is no authority to fine an agency or to remove management.

Approval of Minutes

Upon a motion made and seconded, the minutes of the July meeting were approved.

NMFA Response to Questions, Media Reports and Allegations

Committee members inquired about the responsibility of the NMFA Board in contributing to the current situation. Ms. Winter responded that the board has been very humbled by recent events and that Mr. Balderas has been asked to include the board in his review. Committee members asked to be informed of board decisions that result in changes to the NMFA.

Update on Legislative NMFA Governance Review

Mr. Pollard and Ms. Faust addressed the committee about the contract that the LCS entered into with investment consulting firm Hewitt EnnisKnupp. Mr. Pollard informed the committee that the first priority for Hewitt EnnisKnupp is to examine the ongoing process and to work with the state auditor and Securities Division to prioritize what needs to be accomplished in order to get the NMFA back up and running. Ms. Faust added that the LCS has a good prior working relationship with the chosen firm and that the firm has successfully worked for other agencies in New Mexico.

Committee members discussed whether this contract was filled competitively. Mr. Pollard informed the committee that it was filled on an emergency basis, with the goal being to get the NMFA back on track.

With no further business for the day, the meeting recessed at 4:15 p.m.

Tuesday, August 21

Senator Papen introduced Dr. Robert G. Frank, president of University of New Mexico (UNM). Dr. Frank welcomed committee members to UNM and said that UNM was proud to host the committee.

NMFA Administration of the New Markets Tax Credit Program

Marquita Russel, chief of programs of the NMFA, informed the committee that in 2006, Finance New Mexico, a limited liability company owned by the NMFA, was created to help bolster the economy. The NMFA acts as a managing member and provides staff support. In 2007, Finance New Mexico applied for federal new markets tax credits for the first time and received a \$110 million allocation to finance job-creating businesses, particularly for rural communities and downtown redevelopment projects. Ms. Russel stated that all of the \$110 million allocation has been used. Ms. Russel provided a handout that outlines the transactions that have been closed or that will close soon. She then highlighted a few projects that have been financed through the new markets tax credits programs.

Following the momentum from the first allocation, Finance New Mexico received a second allocation in 2011 for \$46 million, of which three-fourths will be dedicated to rural New Mexico communities, according to Ms. Russel.

Committee members asked about the number of jobs created by the first \$110 million allocation. Ms. Russel informed the committee that approximately 700 jobs were created and that the goal is to generate around 1,200 jobs, which appears possible, with a number of projects near completion. Unfortunately, with the closure of Schott Solar, 250 jobs were eliminated.

Tribal Infrastructure Act Program and Colonias Infrastructure Act Program Reports

Graham Knowles, community services manager of the New Mexico Department of Environment (NMED), informed the committee that in 2005, the Tribal Infrastructure Act was signed into law to ensure adequate financial resources for infrastructure development for tribal communities. Only a federally recognized Indian nation, tribe or pueblo wholly or partially located in New Mexico is eligible to apply for funding under the Tribal Infrastructure Act.

Mr. Knowles informed the committee that in September and October 2011, the Indian Affairs Department and the NMED's Community Services Group developed guidance resources and convened and conducted a series of informational and training workshops that focused on the tribal infrastructure process at six locations around the state. In total, more than 220 tribal administrators, leaders and public officials attended and participated in the workshops.

Mr. Knowles then reviewed the application process as well as the project review and evaluation process. Ultimately, the Tribal Infrastructure Board voted to award \$13 million in support of 28 projects. Of those 28 projects, 14 were fully funded planning/design projects, 12 were fully funded planning/construction projects and two were partially funded design/construction projects. Mr. Knowles informed the committee that from the \$13 million invested, the overall increase in capital investment made by the state is anticipated to be \$36 million. Mr. Knowles also stated that approximately 520 short-term project-specific jobs will be created, and approximately 320 full- or part-time jobs will be created once the funded projects are completed.

Committee members questioned Mr. Knowles about whether the Tribal Infrastructure Board informs a denied applicant about the reasons for denial and what steps it can take to receive funding in the next cycle. Mr. Knowles replied that representatives are sent out into the community to inform applicants of application deficiencies and how they might go forward to receive funding in future cycles. Committee members requested a map of Tribal Infrastructure Fund and Colonias Infrastructure Fund award recipients and projects.

Spaceport Authority Update and Proposed Legislation

Christine Anderson, executive director of the Spaceport Authority, gave an update on the progress of the spaceport. She informed the committee that the spaceport will accommodate four types of customers: the horizontal launch customer, the vertical launch customer, students and tourists. According to Ms. Anderson, the supporting infrastructure is complete; phase one of construction is 99% complete; and phase two of construction is 25% complete.

Ms. Anderson emphasized the need for legislation to reform the Space Flight Informed Consent Act, which currently holds harmless the operators, but not the supply chain, from the tort of negligence and contains a clause to sunset in 2018. Amending the act to hold harmless not only the operators, but also the supply chain and its directors, shareholders and employees and to remove the sunset clause would enable the spaceport to compete with other states for flight providers and customers at no cost to the New Mexico taxpayers. Conversely, failure to

enact the more robust limitation of liability would restrict the spaceport's capacity to be competitive.

Committee members raised questions about a comparable spaceport in Texas and whether that operation has the same overall goals as the New Mexico spaceport. Ms. Anderson replied that while the proposed Texas spaceport tends to be less focused on tourism, its space travel goals align with those of the New Mexico spaceport. She believes that Texas' limitations on tort liability have given it a competitive advantage in attracting flight providers.

Adjournment

There being no further business before the committee, the third meeting of the NMFA Oversight Committee for the 2012 interim adjourned at 12:00 noon.